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IN THE

Supreme Court of the United States

OCTOBER TERM, 1958

No. 202

BEL OIL CORPORATION, *Petitioner*

v.

FEDERAL POWER COMMISSION, *Respondent*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

Bel Oil Corporation, petitioner, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit entered in the above entitled case on April 23, 1958.

JURISDICTION

Jurisdiction to review this case upon writ of certiorari is conferred by 28 USC § 1254(1). The opinion of the Court of Appeals for the Fifth Circuit was filed April 23, 1958.

OPINIONS BELOW

The opinion and order of the Federal Power Commission appear in the Record (R. 3050-3073), and the Commission's order denying rehearing appears in the record at R. 3167. The opinion of the Court of Appeals, printed in Appendix A hereto, is not yet reported.

QUESTIONS PRESENTED

1. Can the Federal Power Commission lawfully issue an order under Section 4(e) of the Natural Gas Act in a proceeding involving an independent producer of natural gas suspending a price which is fixed as to amount and effective date in the contract filed as an initial rate schedule?

2. Was the Federal Power Commission in error in requiring cost of service evidence to determine the reasonableness of a price for natural gas agreed upon initially by the producer and its purchaser?

3. Is evidence of an arm's length contract providing a price which is in the lower range of prices being paid to competing producers in the area and providing a price less than that of competing commodities, sufficient to establish the reasonableness of that price?

STATUTE INVOLVED

The statutory provisions involved are Sections 4(c), (d) and (e) and Section 5(a) of the Natural Gas Act, 15 USC § 717.

STATEMENT

On May 27, 1954, Bel Oil Corporation, hereinafter referred to as "Petitioner" or "Bel", entered into a contract with Transcontinental Gas Pipe Line Corporation, hereinafter referred to as "Transcontinental",

for the sale of gas produced by Bel in the North Elton Field, Allen Parish, Louisiana. (R. 1385-1426). The contract provided for a price of 8.797¢ per thousand cubic feet, excluding a one cent tax reimbursement, for gas delivered from first delivery, July 13, 1954, to November 1, 1954. From November 1, 1954, to November 1, 1959, the contract fixed a price of 16¢ per thousand cubic feet, excluding the one cent tax reimbursement. This price arrangement was demanded by Transcontinental because Transcontinental did not then want to make effective favored nations clauses in contracts covering other gas fields in southern Louisiana (Gale, R. 110). The arrangement was agreed to by Bel because, although Bel had received offers of higher prices from other gas transmission companies (Garrison, R. 136-137), the initial delivery dates under these other contracts were indefinite (Garrison, R. 138). Bel's leases were suffering drainage from wells of other operators and its lessors were demanding protection from this drainage (Field, R. 674; Exhibit, R. 1334).

It is to be noted that there is no "favored nations" clause involved in this proceeding.

After the issuance of Respondent's Order 174-A, Petitioner, protesting the jurisdiction of Respondent and the validity of Order 174-A, applied on September 24, 1954, to make effective the price clause in its contract with Transcontinental. Respondent with design denominated this application a "*supplement*" to Petitioner's contract with Transcontinental (R. 1427), but, as will appear, Petitioner's application did not supplement or change the original Transcontinental contract in any manner whatsoever. By order issued November 4, 1954 (R. 2276), Respondent suspended the effect of

the price clause in Petitioner's contract pending a hearing. The order was subsequently amended to permit Petitioner to collect the sixteen cent price under bond.

Petitioner, over its strong protests as to the jurisdiction of the Commission and as to the validity of Order 174-A, was forced to proceed with this hearing.

At the hearing, Petitioner offered evidence to establish the following: (1) The contract between Bel Oil Corporation and Transcontinental was negotiated at arm's length and in an atmosphere of stiff competition among other producers and other gas purchasers in the southern Louisiana area (Garrison, R. 137); (2) the abnormally low price of 8.797¢ per MCF was really a temporary expedient required by Transcontinental because of the favored nations clauses in its other contracts and accepted by Bel for the short period from July 13, 1954, to November 1, 1954, because Bel's leases were suffering drainage and were in danger of being forfeited (Field, R. 674; Exhibit R. 1334); (3) the sixteen cent price was among the lowest prices paid for natural gas in substantial quantities in southern Louisiana during the period January 1, 1952, to November 1, 1955 (Falck, Exhibits R. 836-860); (4) contracts providing a price of sixteen cents per MCF, effective November 1, 1954, had previously been before the Federal Power Commission, and in Opinions 279 and 280, the Commission determined that the proposed expansion of facilities sought by Transcontinental based on these contracts was in the public interest; (5) even discounting the enhanced value of natural gas as a fuel because of its cleanliness, efficiency and convenience, the sixteen cent price paid by Transcontinental makes gas cheaper on a BTU basis in the

eastern market area than its competitive fuels, coal and oil (Falck, R. 655-658); (6) the sixteen cent price in the Transcontinental contract is less than prices which were being negotiated on or about November 30, 1955, for unregulated intrastate gas sales in southern Louisiana (Vietti, R. 651); (7) the business of producing and selling natural gas involves great risks, is highly competitive, and operates under conditions requiring greater and ever greater expenditures. The prices fixed in the contract involved in these proceedings are necessary to furnish the incentive for exploration vital to the maintenance of adequate gas reserves (Davis, R. 553-559).

On April 2, 1956, after the decisions of this Court in *United Gas Pipe Line Company* v. *Mobile Gas Service Corporation*, 350 U. S. 332, 76 S. Ct. 373 (1956), and *Federal Power Commission* v. *Sierra Pacific Power Company*, 350 U. S. 348, 76 S. Ct. 368 (1956), Petitioner filed a motion to dismiss the proceedings for lack of jurisdiction on the ground that the Federal Power Commission has no authority to prevent the enforcement of a contract made by a natural gas company except under the review powers conferred by Section 5 of the Natural Gas Act (R. 2830). The motion was denied.

In its Opinion No. 300 (R. 3050), the Commission stated the issues as follows:

> "These proceedings present for our resolution the basic question whether the evidence presented by the applicants is sufficient to support a finding that the increased rates of 17¢ per Mcf are just and reasonable within the meaning of the Natural Gas Act. More precisely defined, does the Natural Gas Act permit the Commission to

No.

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approve the increased rates sought to be justified here through evidence of arm's-length bargaining, field prices and commodity or market value of the gas when there is no evidence that the increased rates are not higher than necessary to encourage exploration for and production of known and future gas reserves?"

The Commission concluded:

"The sum total of the evidence presented by the applicants at both hearings demonstrates that the increased rates were reached as a result of arm's-length bargaining and that they are within the range of the field prices in the pricing area in southern Louisiana. It further shows that to exact this price of 17c per Mcf the applicants were required to grant additional considerations to Transcontinental, such as increased dedicated reserves. It is also clear from the evidence presented that the growing demands for gas by Transcontinental's customers in the industrial and heavily populated New York-New Jersey-Pennsylvania area are translated through Transcontinental to increasing demands for gas in the field. The applicants' evidence further tends to establish that the price of gas as sold by Transcontinental to its customers in the New York-New Jersey-Pennsylanvia area competes favorably with the prices of coal and fuel oil for space heating and boiler fuel uses."

and

"Significantly, none of the evidence presented by the applicants is designed to show what rates are needed, either by individual producers or by the industry generally, to further exploration or other production functions. Neither can rates be determined in any way from the evidence before us."

and

". . . We think the recent decision of the Court of Appeals for the District of Columbia Circuit in *City of Detroit* v. *Federal Power Commission*, 230 F. (2d) 810 (C.A.D.C., 1956), certiorari denied, 352 U. S. 829, controlling here.[13]

"[13] It should be remembered that our opinion No. 269, *In the Matters of Panhandle Eastern Pipe Line Company, et al.*, docket Nos. G-1116, et al., issued April 15, 1954, was rendered at a time when the wholesale rates for the sale of gas by independent producers were considered not to be subject to our jurisdiction. In such a context, the economic and legal considerations impelling our action were different from those in the case now before us where all interstate wholesale rates are subject to our regulatory jurisdiction.

In referring the case back to the Commission for the taking of additional evidence, the Court held that in rate making the Commission must always 'relate its action to the primary aim of the Act to guard the consumer against excessive rates. If the Commission contemplates increasing rates for the purpose of encouraging exploration and development, . . . it must see to it that the increase is in fact needed, and is no more than is needed, for the purpose. Further than this we think the Commission cannot go without additional authority from Congress.' *Id.* at 817.

"We think it is plain from the language of the *City of Detroit* case, supra, that the value method used alone, as proposed by the applicants, is not a method of rate making open to us within our delegated power. 'For, though we hold that [the conventional rate-base] method not to be the only one available under the statute, it is essential in such a case as this that it be used as a basis of comparison. It has been repeatedly used by the Commission, and repeatedly approved by the courts, as a means of arriving at lawful—"just and reasonable"—rates under the Act. Unless it is

continued to be used at least as a point of departure, the whole experience under the Act is discarded and no anchor, as it were, is available by which to hold the terms "just and reasonable" to some recognizable meaning."[4] This record contains nothing which could be used as the basis of comparison found essential by the Court."

"[4] 230 F. (2d) 810, 818-819."

The Commission found that the 16c per MCF embodied in Petitioner's contract for gas delivered beginning November 1, 1954, constitutes a change in rate within the meaning of Section 4 (d) and (e) of the Natural Gas Act, and that the rate-making authority delegated to the Commission under the Natural Gas Act does not empower the Commission to determine reasonable rates on the basis of arm's-length bargaining and market value alone without evidence that the rates are no higher than necessary to encourage exploration for and production of known and future gas reserves of Petitioner.

The court below granted the petition to review "to the extent that the Commission is directed to reopen these proceedings to afford petitioners reasonable opportunity to adduce such evidence as they may be advised is relevant to the inquiry whether the proposed rate of 16 cents plus 1 cent state tax is just and reasonable." In all other respects the petition was denied.

REASONS RELIED ON FOR GRANTING THE WRIT

This case presents the important question of whether the Commission can suspend a price agreed upon in an original contract between an independent producer and a purchasing pipeline company filed with the

Commission as an initial rate schedule. Petitioner contends that the exercise of such authority by the Commission in the circumstances here is contrary to the interpretation of the statute by this Court in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332. Further, in this case, involving an independent producer of natural gas, there has been a misapplication of the decision in *City of Detroit* v. *F.P.C.*, 230 F. 2d 810, cert. denied 352 U. S. 829, which involved the proof required in a proceeding in which there was no contract between non-affiliates as presented here.

I. The Case Involves an Important Question Concerning the Statutory Authority of the Commission to Issue Suspension Orders

The price of 16¢ per MCF which was the subject of the suspension order of the Commission was in the original contract entered into May 27, 1954. This 16¢ price, to be effective November 1, 1954, is part of the original agreement of the parties. Notwithstanding this fact, both the Commission and the court below considered the 16¢ price as a "change" in rate schedule subject to the Commission's power of suspension under Section 4 of the Act. The Commission attempted to distinguish the *Mobile* case, supra, but the court below did not even refer to that case. Instead, it relied upon an earlier decision of its own involving a "favored nations" clause and a decision of the Tenth Circuit which was rendered virtually simultaneously with *Mobile* and did not even refer to or discuss it.[1]

[1] The cases relied upon by the court below were *Mississippi Power & Light Co.* v. *Memphis Natural Gas Co.*, 5th Cir., 162 F. 2d 388, cert. denied 332 U. S. 707 and *Cities Service Producing Co.* v. *Federal Power Commission*, 10th Cir., 233 F. 2d 726.

In the *Mobile* case, the Court said that the Natural Gas Act, "evinces no purpose to abrogate private rate contracts as such," but on the contrary, "the Act expressly recognizes that rates to particular customers may be set by individual contracts." The rights of natural gas companies to make initial rates and prices "remain undefined and unaffected by the Act." In its *Mobile* decision this Court also stated that under the regulatory scheme of rates contemplated by the Natural Gas Act "* * * all rates are established by the natural gas companies, by contract or otherwise * * *," and that the Act "purports neither to grant nor to define the initial rate-setting powers of natural gas companies." This Court emphasized in its *Mobile* decision that the Act is designed to preserve the integrity of contracts thus insuring the stability of supply arrangements.

Under the clear holding in the *Mobile* case, Petitioner had the right to negotiate its contract here involved and to provide therein for the price to be paid for its gas for the entire period of the contract. Such contract and all the provisions thereof became Petitioner's initial rate schedule. The price involved was an integral provision of the original contract and a part of the initial price.

The authority of the Commission to suspend under Section 4 (e) of the Act is limited to "changes" in rates or prices. The Commission's own rules recognize that Section 4 (e) is only applicable to "changes" as Sections 2.4 and 2.52 of its General Rules and Regulations provide "An initial rate schedule cannot be suspended" (12 F. R. 8470, 13 F. R. 8259).

In its *Mobile* decision this Court made clear the limited authority of the Commission under Section

4 (e) of the Act. The Court referred to Section 5 (a) as containing the "basic power" of the Commission and stated that all Section 4 (e) added was the further power to suspend "a *newly* changed rate or contract." This Court also held that the statute dealt with "agreed-upon" changes to a contract made by "mutual agreement."

The contract here involved was negotiated and entered into in its entirety. No *change* has ever been made by the parties to that contract. The suspension proceeding here does not involve a "newly" changed price by any act of the parties; nor any "agreed-upon change" in the price provision by "mutual agreement" of the parties. No agreement of the parties was entered into after the filing of the original contract as the initial rate schedule. Accordingly, there was no "newly" changed price before the Commission subject to suspension. The price of 16c per MCF effective November 1, 1954 was agreed to May 27, 1954.

By promulgating Section 154.94 (e) of its rules, the Commission has attempted to avoid the requirements of Section 5 (a). That section of the Commission's rules provides that "The operation of any provision of the rate schedule providing for future or periodic changes in the rate, charge, classification, or service after June 7, 1954, * * * shall constitute a change in rate schedule" (R. 9597; 9603). The Commission cannot enlarge its powers under Sections 4 and 5 of the Act by the promulgation of rules. In *Manhattan General Equipment Co. v. Commissioner of Internal Revenue*, 297 U. S. 129, 134-5, this Court pointed out that a "regulation which * * * operates to create a rule out of harmony with the statute, is a mere nullity."

By calling the 16c per MCF price in Petitioner's contract a "change" in its initial rate schedule, the Commission has sought to escape the burden of proof imposed upon it by Section 5 (a) and to require Petitioner to assume the Section 4 (e) burden of proof required of natural gas companies which file "changes" in their rate schedules. Such action is clearly contrary to the Natural Gas Act, Section 7 (c) of the Administrative Procedure Act and the procedural due process clause of the Fifth Amendment to the Constitution of the United States.

II. The Case Involves a Misapplication of the Decision in City of Detroit v. Federal Power Commission

The Federal Power Commission erroneously relied upon the decision of the Court of Appeals for the District of Columbia Circuit in *City of Detroit* v. *Federal Power Commission*, 230 F. 2d 810, cert. denied 352 U. S. 829 in support of its action in dismissing the rate proceedings involving Petitioner. The court below referred to the Commission's reliance upon this decision but did not expressly hold that it was inapplicable.

In the *City of Detroit* case the Court held, in a pipeline case, that in such a case "rate base" or "cost of service" evidence must be used as a basis of "comparison" with fair field price or commodity value evidence. The *City of Detroit* case was not a proper precedent for use by the Commission to justify its action because that case related solely to pipeline-produced gas and specifically was not intended to be applicable to an independent producer such as Petitioner. There was no contract between non-affiliates involved there. The price used there was simply a

bookkeeping transaction on Panhandle's books. The Circuit Court in the *City of Detroit* case meticulously pointed out, in various places in its opinion, that it was dealing solely with pipeline-produced gas. Thus, the Court states that (230 F. 2d at p. 818):

> "* * * We simply say that if the Commission is now to abandon the treatment historically accorded *pipeline-produced gas* in rate making on the ground that the ultimate public interest will be better served thereby, the Commission should justify it on the record." (Italics supplied.)

With respect to the Commission's reliance upon the desirability of pipeline companies owning their own producing facilities, thus increasing their bargaining power in connection with gas purchases, the Court states that (230 F. 2d at p. 817):

> "* * * If the Commission contemplates increasing rates for the purpose of encouraging exploration and development, or the ownership *by pipeline companies* of their own producing facilities, it must see to it that the increase is in fact needed, and is not more than is needed, for the purposes." (Italics supplied.)

Again, the Court specifically differentiated between pipeline companies and independent producers with respect to the risks of exploration and development. The Court said (230 F. 2d at p. 818, footnote 12):

> "If the Commission were uniformly to apply the field price system, all risks of exploration and development would be placed upon the pipeline companies. On the other hand, if the Commission gives the companies their option, the traditional rate-base system would naturally be chosen whenever costs of production exceed the field price. In

that event, no risks of exploration, development, or production would fall upon the companies, and it would appear that a small margin of profit should suffice to encourage such activities. *It is doubtful that the same margin of profit would be required as might be received by producers who bear their own risks. Yet the field price system would seem to have the effect of putting pipeline companies on a par with such producers.*"

(Italics supplied.)

In the *City of Detroit* case the Court was fully aware of the decision of this Court in the case of *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, because it referred to that decision and stated that the Commission should, upon remand, consider its impact upon the Commission's "stated reasons for desiring to encourage pipeline companies to produce their own gas."

The attempt to apply the *City of Detroit* case to independent producers, in spite of the carefully worded language of the Court specifically restricting its application to pipeline companies, results in a complete misinterpretation of the meaning of that decision. It is abundantly clear, as the Court repeatedly stated, that it dealt only with a pipeline case where the Commission had departed from the historical treatment of pipeline-produced gas. Independent producers were in no manner involved and as a matter of fact were specifically distinguished from pipeline companies by the Court itself.

In the case of independent producers, there has never been a "historical" nor any other method of Commission regulation from which to "depart." The Commission is at the threshold of its regulation of independent producers, and we submit is legally free to

adopt the commodity value method of regulating producer prices.

The decisions of this Court, particularly in *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U. S. 575; *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591 and *Colorado Interstate Gas Co.* v. *Federal Power Commission*, 324 U. S. 581, have held that the Natural Gas Act provided no "formula" by which a "just and reasonable" rate is to be determined. In the *Colorado Interstate* case this Court, dealing specifically with the question whether "the fair field price of the gas as a commodity" could be allowed instead of cost, stated that:

> "* * * We do not say that the Commission lacks the authority to depart from the rate-base method."

In the *City of Detroit* case the foregoing cases were reviewed and the Court concluded that, even in the case of pipeline companies, the fair field price, instead of the traditional rate-base method, was lawful. As a matter of fact, the Commission itself recognizes that it may legally allow fair field price to pipeline companies, in lieu of cost, because it has recently done so in its order of May 15, 1957, *In the Matter of Olin Gas Transmission Corporation*, Docket No. G-8559 (17 F.P.C. 685).

In its recent decision in *Mississippi River Fuel Corp.* v. *Federal Power Commission*, 252 F. 2d 619, cert. denied 2 L. ed. 2d 260, the Court of Appeals for the District of Columbia Circuit (the same court which decided the *City of Detroit*) dealt only with "pipeline company" produced gas. The Court considered the 100 per cent-owned producing affiliate, involved in that

decision, as standing "in the same position as does the intergrated producing 'arm' for a pipeline company." An "independent" non-affiliated producer, which this record established Petitioner to be, was again not before the Court. And, as stated, the Court was again careful to point out that the *City of Detroit* case dealt only with a "pipe-line company" producing its own gas.

It thus appears clear that the Commission has misinterpreted and misapplied the decision of the Court in the *City of Detriot* case. The Commission, under that case and the decisions of the Supreme Court in the *Natural Gas Pipeline, Hope* and *Colorado Interstate* cases, may lawfully adopt for independent producers a commodity value method of regulation, such as here developed by Petitioner. By its misinterpretation and misapplication of the *City of Detroit* case the Commission has abrogated the function which Congress intended it to perform and has attempted to avoid its responsibilities under the Natural Gas Act.

Petitioner offered adequate, sufficient and uncontradicted evidence supporting the reasonableness of its price, which was rejected by the Commission because of its misinterpretation of the *City of Detroit* decision. Under the circumstances, Petitioner's price should have been determined to be just and reasonable and the Commission's order should be set aside because of its failure to make that finding.

CONCLUSION

This case presents important questions of interpretations of the natural Gas Act and the Federal Power Commission's jurisdiction and authority thereunder.

For these reasons, the petition for certiorari should be granted.

Respectfully submitted,

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APPENDIX A

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 16581

BEL OIL CORPORATION, *Petitioner*,

v.

FEDERAL POWER COMMISSION, *Respondent*.

No. 16583

UNION OIL COMPANY OF CALIFORNIA, and THE LOUISIANA LAND AND EXPLORATION COMPANY, *Petitioners*,

v.

FEDERAL POWER COMMISSION, *Respondent*.

No. 16584

MORRIS RAUCH, ET AL., *Petitioners*,

v.

FEDERAL POWER COMMISSION, *Respondent*.

Petitions to Review Orders of the Federal Power Commission.

(April 23, 1958.)

Before TUTTLE, JONES and WISDOM, Circuit Judges.

TUTTLE, Circuit Judge: These petitions, presented on a single record, seek review of an order of the Federal Power Commission, Opinion No. 300, reported at 16 F.P.C. 100-118, dismissing certain rate filings of the petitioners as independent producer natural gas companies.[1] The rate

[1] In view of the holding by this Court in Deep South Oil Co. v. F.P.C., 5 Cir., 247 F. 2d 882; Shell Oil Co. v. F.P.C., 247 F. 2d 900, cert. den. 355 U.S. 930; Humble Oil & Refining Co. v. F.P.C., 5 Cir., 247 F. 2d 903, cert. den. 355 U.S. 930; and Continental Oil Co. v. F.P.C., 5 Cir. 247 F. 2d 904, we do not give further consideration to the contention that these are not natural gas companies within the purview of the Natural Gas Act, 15 U.S.C.A. 717.

increases would have been from 8.79 cents to 16 cents per Mcf, plus a 1 cent state tax.

On June 9, 1954, the three parties all had contracts with Transcontinental Gas Pipe Line Corporation (Transco), under which they agreed to furnish certain minimum quantities of gas for a period of twenty years, for which the price was fixed "temporarily" at 8.7915 cents per Mcf until November 1, 1954, and 16 cents per Mcf thereafter, with an automatic escalation of one cent every five years. It was on June 7, 1954, that the Supreme Court decided *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672. The Commission subsequently, by Orders 174, 174A and 174B permitted all independent natural gas companies engaged on or since June 7th in jurisdictional sales to file their rates in effect on that date without any supporting data to justify any increases that had theretofore been put into effect. The companies were permitted to file copies of their contracts in lieu of detailed rate schedules.

Petitioners filed their contracts, all of which provided for an automatic increase, on November 1, 1954. Two of the petitioners also filed notice of the increase to 16 cents. The Commission thereupon ordered all of these increases suspended under the authority of Section 4(e) of the Act. After the period of suspension the rates were permitted to go into effect under the terms of the Act which require reimbursement by petitioners if they should not ultimately be entitled to the rate charged.

A number of local distributing companies and state commissions intervened to oppose the rate increase and Transco intervened on behalf of the petitioners.

After several postponements, urged by petitioners, extended hearings were held. In general it can be stated that the evidence offered by petitioners consisted of proof of the competitive conditions in the Louisiana fields, the contracts negotiated by petitioners and others in that field,

and evidence that the contracts were negotiated at arm's length. After the presentation was concluded, without any cross examination or counter proof by interveners, a motion was made to dismiss on the ground that applicants had not sustained their burden of proof that the higher rate was "just and reasonable."

The Commission entered its "Order Postponing Action on Motion to Dismiss and Referring Proceedings to Examiner" in which it said:

> ". . . The fact that contracts have been entered into in good faith and in arm's-length bargaining does not make them immune from the regulation in the public interest prescribed by Congress, nor are producer contract terms per se an indication that the prices agreed upon are just and reasonable either initially or as subsequently increased pursuant to escalation clauses or otherwise. (See Colorado Interstate Gas Co. v. F.P.C., 142 F. 2d 943, 953 (C.A. 10, 1944), aff. 342 U.S. 581; Mississippi River Fuel Corp. v. F.P.C., 121 F. 2d 159, 163 (CA. 8, 1941).)
>
> "The exhibit submitted by applicants to show relative field prices is merely a numerical listing of contract prices for gas sold within the pricing area and is insufficient to justify the proposed increases.
>
> "It may be observed that in providing for Commission responsibility in connection with rate filings the Natural Gas Act makes no distinction between independent producers and interstate pipeline companies. If they are subject to the Act, the same criteria and procedures are prescribed for rate-fixing purposes, since both classes are natural gas companies under the Act. The Commission is free, within the ambit of its statutory authority in rate fixing, to make the pragmatic adjustments which may be called for by particular circumstances (F.P.C. v. Natural Gas Pipeline Co., 315 U.S. 575, 586). While it is true that the source of our authority over rates of independent producers is contained in Sections (4) and (5) of the Natural Gas Act, we do not say that in fixing the rates of natural gas companies which are independent producers we are compelled to apply the same formula as that ap-

plied in fixing the rates of natural gas companies which are interstate pipeline companies.

"In dealing with the rates of interstate pipeline companies, we have pointed to the burden placed by Section 4(e) of the Act upon those natural gas companies seeking approval for rate increases and in appropriated cases have pointed to the failing of some companies to present evidence which would justify the increases, for which reason we have denied applications for approval, and in these actions we have judicial approval. (Mississippi River Fuel Corp. v. F.P.C., 121 F. 2d 159, 165 (C.A. 8, 1941).) The independent producers which are applicants herein are under the same burden as interstate pipeline companies to justify any proposed rate increases, even if their operations may differ.

"Upon consideration of all of these matters and the evidence so far presented, we would be required to grant the motion to dismiss and to terminate these proceedings, for the evidence does not show that the requested increased rates would be just and reasonable. Nevertheless, solely because this is the first series of cases involving the rates of independent producers upon which we have acted, we will allow Applicants a further period of time beyond which we do not propose to extend the resumption of the hearing, rather than granting the motion to dismiss forthwith.

. . . .

"The Applicants should now be fully prepared to demonstrate the lawfulness of the proposed increases or we must deny the applications and dismiss the proceedings. Reasonable consideration of the rights of the other parties and of the general public will justify no further delays."

Upon the reconvened hearing petitioners introduced additional evidence tending to show that petitioners did not possess any dominating position in the industry, that natural gas is competitive with other non-regulated fuels, that the proposed prices were comparable with unregulated prices for local consumption; that maintenance of such a price is necessary to provide appropriate incentives for ex-

ploration and production of nautral gas in Louisiana. No evidence was offered to show the actual cost of service to the producers—that is no evidence as to any economic factors related to their financial interests or needs, none as to operating expenses or capital costs, as to the return or profits they were earning under the 8.79 cent rate or which they would earn under the 16 cent rate, no evidence to indicate whether the rate was necessary to maintain credit and to attract capital. It can fairly be assumed, we think, that the failure to adduce such evidence was part of petitioners trial strategy to make more persuasive their argument in favor of a field price basis, for rate purposes, for in the brief of Union Oil is the following statement:

> "It was the judgment of petitioners that evidence of that type would have led to confusion in the presentation of their case and prejudiced the chances of acceptance by the Commission of the principles which petitioners urged on the commission as the proper basis of regulation."

Because of the absence of the financial type of evidence, a motion was again made for a dismissal of the application. The Commission referred the case back to the Examiner to make his report, the record was opened for cross examination by interveners, which they waived, and thereafter the Examiner filed his report recommending dismissal because of the failure of petitioners to make out a prima facie case of reasonableness. The Commission, two members dissenting, held that there was a failure to make out a prima facie case of just and reasonable rate and granted the motion to dismiss. The Commission, for the first time, gave a strong indication of what it considered to be essential in the proof of just and reasonable rates. It said:

> "We think the recent decision of the Court of Appeals for the District of Columbia circuit, in City of Detroit v. Federal Power Commission, 230 F. 2d 810, cert. den. 352 U.S. 829, is controlling here."

That part of the City of Detroit decision germane to the Commission's discussion is:

> "For, though we hold that method [the rate base or cost of service method] not to be the only one available under the statute, it is essential in such a case as this, that it be used as a basis of comparison. It has been repeatedly used by the Commission, and repeatedly approved by the courts, as a means of arriving at lawful—'just and reasonable' rates under the Act. Unless it is continued to be used at least as a point of departure, the whole experience under the Act is discarded and no anchor, as it were, is available by which to hold the terms 'just and reasonable' to some recognizable meaning."

Following the order of dismissal, petitioners filed motions for rehearing and asked that the matter be referred once against to the examiner to permit petitioners to tender evidence of cost of service. The motions were denied.

Petitioners strongly contend that they urged the field price, or cost of commodity, evidence as adequate to support a finding of a just and reasonable rate in the best of faith, relying in great part, so they say, on representations to that effect by the Commission itself. They say the Commission in the Panhandle Eastern Pipe Line Co. case, Opinion No. 269, which is the case later reversed by the Court of Appeals for the District of Columbia Circuit, quoted from above sub nom. *City of Detroit* v. *Federal Power Commission*, valued the natural gas produced by an interstate pipe line company for rate making purposes on the basis of fair field price rather than on the basis of a calculated rate of return on the company's investment in its producing properties. They say that in applying to the Supreme Court for certiorari in the City of Detroit case, the Commission still stood on the field price theory of rate making. They also point out that the Commission, in

its 1956 Report to Congress,[2] recommended an amendment to the Natural Gas Act as follows:

> "A standard for pricing or evaluating natural gas as a commodity which would not require use of a rate base or traditional utility ratemaking principles, but which would enable the Commission to weigh the interests of the consumer in low prices with the necessity of providing assurance of future gas supplies;".

Petitioners argue from this record and in light of these circumstances, together with the broad scope which the Supreme Court says resides in the Commission in its ascertainment of a just and reasonable rate, first that the evidence was sufficient to establish a prima facie case, and second, if not, it excused their failure to offer the cost of service evidence at the two hearings and the case should be remanded to the Commission to permit them to do so.

In support of the first position, petitioners cite *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591:

> "Congress, however, has provided no formula by which the 'just and reasonable' rate is to be determined. 320 U.S. 591, 600.

The Court also said:

> "We held in Federal Power Commission v. Natural Gas Pipeline Co., supra, that the Commission was not bound to the use of any single formula or combination of formula in determining rates. Its rate-making function, moreover, involves the making of 'pragmatic adjustments.' Id. p. 586. And when the Commission's order is challenged in the courts, the question is whether that order 'viewed in its entirety, meets the requirements of the Act. Id., p. 586. Under the statutory standard of 'just and reasonable' it is the result reached not the method employed which is controlling. Cf. Los Angeles Gas & Electric Corp. v. Railroad Commission, 289 U.S. 287, 304-305, 314; West Ohio Gas Co. v. Public Utilities Commission (No. 1), 294 U.S. 63, 70;

[2] 1956 Annual Report of the Federal Power Commission, p. 19.

> West v. Chesapeake & Potomac Tel. Co., 295 U.S. 662, 692-693 (dissenting opinion). It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end." 320 U.S. 591, 602.

See also in this connection, *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U.S. 575, 586, and *Colorado Interstate Gas Co.* v. *Federal Power Commission*, 324 U.S. 581.

We cannot agree that these cases are authority for the proposition that the evidence thus far adduced makes out a prima facie case of reasonableness of the contract price of 16 cents. We do not hold that evidence of field price is irrelevant. We do hold that evidence of unregulated prices in the field is not sufficient to warrant a finding by the Commission that a price comparable to them is just and reasonable within the intendment of the Natural Gas Act. Neither is evidence of the field price when coupled with the opinion of experts that the price must be high enough to provide an incentive for exploration and development of new sources of supply.

Our attention has been called to the opinion and order issued on April 4, 1958, in the matter of Pan American Petroleum Corp., et al, Opinion No. 310, in which the Commission has found just and reasonable an increased rate from 75 to 85 cents per Mcf for an Oklahoma field without requiring proof of cost of service. Without having the record of that case before us, it is apparent that the Commission has nevertheless withdrawn somewhat from the generality of its holding that a rate-base method must in all events be used at least as a point of departure. Recognizing, however, as we do that the rate increase there was an extremely modest one, we do not conclud from that order that the Commission intends to abandon its position taken as to the petitioners here. In fact the opinion seeks

to distinguish these cases. Some of the points of distinction are not, we think, significant. Without deciding that the rate-base method is essential in every rate case, we agree that the Commission did not have sufficient evidence before it to approve these rates as just and reasonable.

Upon the second position taken by the petitioners, however, we conclude that the Commission erred in the particular circumstances of these proceedings in not reopening the hearings once again to permit the petitioners to introduce evidence of a rate base which in its written opinion, after the close of the hearing, the Commission said for the first time is an essential part of such an inquiry. We fully share the Commission's conclusion that petitioners were not unaware during the two years of pendency of the matter that evidences of cost of service might in the end be an important part of the proof they would have to make. The Commission takes the position that, with ample warning of the inadequacy of their proof, the failure of petitioners to come forward with such evidence amounted to a calculated gamble by them which they lost, and that they should not be entitled to another opportunity to make out their case. If indeed petitioners made such a gamble, it was an expensive one. If this order stands, the petitioners in this and other cases dealt with by the Court at this time, are required to account for to their customers a substantial sum of between seven and eight million dollars, all or part of which they may really be entitled to keep if their proof finally wins the approval of the Commission of a higher rate. In such circumstances some parties would be unjustly enriched and petitioners would be heavily penalized without reference to the real merits of the controversy.

The regulation of the prices at which thousands of "natural gas companies" may sell to the pipe line companies is a difficult one at its best. It is a field which in many respects requires new formulas to test what is just and reasonable. We think it would be an unjust penalty if

we were to apply too strict a rule as to the reception of evidence in such a case. This is clearly demonstrated by order No. 310 in Pan American Petroleum Corporation referred to above. We think it quite clear that in light of that order the Commission might adopt some pragmatic standard to apply to these cases as it did with Pan American, et al.

Holding as we do that the proof was insufficient but that reasonable opportunity should be given to petitioners to bring forth additional proof, we think that we need not notice many of the other contentions of petitioners at this time. We do, however, hold that in line with our previous cases cited in footnote 1, *supra*, these petitioners are "independent producers" and "natural gas companies" and their sales are subject to regulation under the Act.

We also conclude that even though the increases here in issue had been predetermined by contract before the Supreme Court's decision of the Phillips case and thus before the cut-off-date of June 7, 1954, they are "rate changes" subject to Section 4(d) of the Act[3] and not an initial rate subject to changes under Section 5(a) of the Act. Section 5(a) places the burden on the Commission or other moving party to prove the initial rate unjust or unreasonable. We passed on a similar question in *Mississippi Power & Light Co.* v. *Memphis Natural Gas Company*, 5 Cir., 162 F. 2d 388, cert. den. 322 U.S. 770, where the contract had a "favored nation" clause in it under which the consumer com-

[3] "Rates and charges; Schedules; Suspension of New Rates. Sec. 4.

. . . . .

"(d) Unless the Commission otherwise orders, no change shall be made by any natural gas company in any such rate, charge, classification, or service, or in any rule, regulations, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published."
15 U.S.C.A. §717(c)(d).

pany contended it was entitled to an automatic reduction in rate. We said there:

> "The 'favored nation' clause became inoperative after the passage of the Natural Gas Act. Section 4 therof provides: '. . . every natural-gas company shall file with the Commission . . . schedules showing all rates and charges for any transportation or sale . . .' and 'no change shall be made by any natural-gas company in any such rate . . . except after thirty days' notice to the Commission and to the public . . .'
>
> "Rate making is a legislative function that the courts will not interfere with, at least until the Commission has exercised the function. To give effect to the 'favored nation' clause would operate to transfer the legislative function of rate-making from the Commission to the courts."

See also *Cities Service Gas Producing Co.* v. *Federal Power Commission*, 10 Cir., 233 F. 2d 726.

What we have said with respect to the new rate being a change within contemplation of the Act also answers the complaint by petitioners that the Series 174 orders of the Commission are invalid as applied to them in view of the fact that they had already contracted for the increases prior to June 7, 1954. As pointed out in *Cities Service Gas Producing Co.* v. *Federal Power Commisison*, *supra*, the Act itself forbids any changes in rates except under the terms of the Act. So far as is here relevant, all the 174 orders do is to implement this provision of the statute.

Other contentions of petitioners whose resolution is not implicit in the decision we now make, are not now passed upon but will await the completion of the record before the Commission.

The petition is granted to the extent that the Commission is directed to reopen these proceedings to afford petitioners reasonable opportunity to adduce such evidence as they may be advised is relevant to the inquiry whether the proposed rate of 16 cents plus 1 cent state tax is just and reasonable. In all other respects the petition is

DENIED.

Judgment

Extract from the minutes of April 23, 1958.

No. 16581

BEL OIL CORPORATION

v.

FEDERAL POWER COMMISSION

This cause came on to be heard on the petition of Bel Oil Corporation for a review of an order of the Federal Power Commission issued on February 6, 1957 in Docket No. G-4505, and was argued by counsel;

On consideration whereof, It is now here ordered, adjudged and decreed by this Court that the petition for review in this cause be, and the same is hereby, granted to the extent that the Commission is directed to reopen these proceedings to afford petitioner reasonable opportunity to adduce such evidence as it may be advised is relevant to the inquiry whether the proposed rate of 16 cents plus 1 cent state tax is just and reasonable; and in all other respects that said petition be, and it is hereby, denied.